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SUBJECT: FINANCE MINISTER DECLARES NEW BEGINNING FOR CREDIBLE AND
TRANSPARENT MINISTRY OF FINANCE

REF: A) Kabul 3701
B) Kabul 3714
C) Kabul 2812

¶1. (SBU) Summary: On November 14, Finance Minister Zakhilwal told U.S. Treasury Deputy Assistant Secretary for Technical Assistance Policy Larry McDonald and Ambassador Wayne that the U.S. Treasury's technical assistance support had helped strengthen his Ministry's credibility and transparency. Minister Zakhilwal said corruption is a serious challenge within MoF but reiterated his determination to eradicate it. He also stressed his hope to focus on several top reforms in the year ahead that will improve service delivery to the population. Zakhilwal asked that more resources be channeled through Afghanistan's core budget since public financial management systems are now sound enough to handle larger inflows. Minister Zakhilwal credited U.S. support as being crucial to GIROA's negotiations with the IMF and in the HIPC debt relief process. End summary.

SEEKING DEMAND-LED GROWTH IN TECHNICAL ASSISTANCE

¶2. (SBU) Visiting DAS McDonald confirmed Treasury's ongoing commitment to Afghanistan and asked the Minister about additional needs for technical assistance. The Minister requested assistance to strengthen the audit functions in the Ministry of Finance's (MoF) Budget and Treasury departments and provincial Ministry offices (Mustofiats). Minister Zakhilwal stated that Treasury support has been critical to modernizing the budget process in his Ministry. Moving forward, he would like to see the budget become more innovative and include incentives. Internal audit capacity needs to be significantly strengthened before the MoF can take full advantage of the recent reinstatement of Article 61, a World Bank Afghanistan Reconstruction Trust Fund (ARTF) benchmark which enables MoF to audit other GIROA agencies. Minister Zakhilwal also wants to implement a new tax collection system within the Provincial Mustofiats whereby revenues are remitted to the Revenue Department instead of to the Administration Department, both under the Ministry of Finance. He emphasized that growth in technical assistance should be demand-driven and organic.

NEW REFORM AGENDA TO COMBAT CORRUPTION

¶3. (SBU) Minister Zakhilwal stated that Afghanistan is on a path toward a "new beginning," emphasizing the need to improve the donor community's trust in GIROA. Once the new Cabinet is established, he will begin work on a reform package that will be driven by the GIROA and supported by the U.S.

¶4. (SBU) In response to Ambassador Wayne's question on the reform agenda, Minister Zakhilwal said he will propose a plan at the next Joint Coordination Management Board (JCMB) meeting to use funds from the Civilian Technical Assistance Plan (CTAP) (ref: Frej/Z cable) to carry out targeted reforms at the top 5-6 ministries responsible for 80-90% of GIROA's economic development initiatives. He said reforms will focus on up to ten areas selected by the potential to increase

service delivery, reduce corruption, and increase government revenue.

15. (SBU) Minister Zakhilwal emphasized the importance of building capacity in tax collection and non-tax revenue. Non-customs revenue from the provinces remains very low. While improving tax collection capacity is more difficult than increasing customs capacity, it will provide a more sustainable source of revenue over the long term. The Minister will also enforce stronger collection efforts on such high money flow areas as wedding halls, rents in expensive neighborhoods in Kabul, and large international companies.

16. (SBU) Minister Zakhilwal highlighted the recent anti-corruption success of firing customs officials at the Kabul Airport. These high-ranking airport administrators are currently on administrative leave and likely to be replaced. Minister Zakhilwal said that he monitored the case himself after receiving two tips (one from the U.S. Embassy), and he estimated that \$30-50 million dollars may have been diverted from government coffers by the alleged offenders.

17. (SBU) Note: This law enforcement action was handled by Minister Zakhilwal's personal bodyguards, who had no formal authority to make arrests. This raises a red flag that Afghan officials may be prone to using extra-legal methods to combat corruption. Such methods can produce quick results but ones that may not stand up in a court of law. Zakhilwal told Ambassador Wayne that he had called Interior Minister Atmar to get a proper investigation under way. End note.

LIMITING TAX EXEMPTIONS ON FOREIGN FIRMS

18. (SBU) Minister Zakhilwal stated that large international contractors hired by U.S. and other foreign assistance agencies have

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sought unwarranted and excessive tax exemptions that protect their profits from sales to non-assistance-related activities. He believes that his Revenue and Customs Departments have granted 50-60% more tax exemption than is appropriate. Moving forward, he stated that MoF needs to know specific details of each foreign assistance contract to ensure international firms are not exploiting their tax-exempt status.

19. (SBU) Note: The U.S. mission has noticed an uptick in putative MoF enforcement measures against contractors, many of which violate the terms of bilateral agreements between the USG and Afghanistan. We are able to resolve most issues at the working level, but it is clear the MoF sees contractors, who are fully tax-exempt under the Status of Forces Agreement and other bilateral agreements, as potential sources of revenue and will continue to explore the limits of the broad existing agreements. (Note: In a conference in Kuwait last year, the military committed to a principle of sharing contracts and contract values with Afghan Ministry of Finance, to ensure that local firms winning business opportunities would pay appropriate taxes). End note.

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